UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF MONTANA

In re **ROBERT D. SMITH, SR.** and **CAROL L. SMITH**, Debtors.	Case No. **04-62741-13**

MEMORANDUM of DECISION

At Butte in said District this 7th day of January, 2005.

In this Chapter 13 bankruptcy, after due notice, a hearing was held December 7, 2004, at Butte on confirmation of Debtors' Amended Chapter 13 Plan filed December 4, 2004, together with the Trustee's objection thereto. The Debtors Robert Smith ("Robert") and Carol Smith ("Carol") appeared at the hearing and testified, and were represented by attorney R. Clifton Caughron. The Chapter 13 Trustee, Robert G. Drummond, appeared at the hearing in opposition to confirmation of Debtors' Amended Chapter 13 Plan. In particular, the Trustee argues that Debtors are failing to commit all their disposable income to their plan as required by 11 U.S.C. § 1325(b)(1) and that Debtors are unreasonably discriminating among creditors as prohibited by U.S.C. § 1322(b)(1). Exhibits A, B and C were admitted into evidence without objection. At the conclusion of the hearing, the Court took confirmation of Debtors' Amended Chapter 13 Plan under advisement. The Court has reviewed the record and applicable law and this matter is ready for decision. For the reasons discussed herein, the Trustee's objections are sustained and confirmation of Debtors' Amended Chapter 13 Plan is denied.

Debtors' Amended Chapter 13 Plan provides for payments of $150.00 per month for 19 months and $291.00 per month for 17 months, for total plan payments of $7,797.00 over the life of Debtors' 36 month plan. The Trustee filed an objection to confirmation of Debtors' Amended Chapter 13 Plan on October 12, 2004, arguing that Debtors' Amended Plan is not entitled to confirmation because: (1) Debtors propose to pay a student loan creditor outside the Plan separately from the class of unsecured creditors, which the Trustee contends unfairly discriminates among creditors in a class in violation of 11 U.S.C. § 1322(b)(1); (2) that payments of $141.00 per month for a period of 19 months on a horse trailer used in Debtors' horse training and roping business, which operates at a loss, is not reasonably necessary for the maintenance of Debtors' household and must thus be included in Debtors' disposable income calculation pursuant to 11 U.S.C. § 3125(b)(1)(B); and (3) that Debtors should have to include the other business expenses set forth on Schedule J, which the Trustee contends are understated, in the disposable income calculation because, as asserted earlier, Debtors operate their horse training and roping business at a loss.

This is a core proceeding under 28 U.S.C. § 157(b)(2)(L) involving confirmation of a plan. At issue is: (1) whether Debtors' Amended Chapter 13 Plan discriminates unfairly against the class of unsecured claims in violation of § 1322(b)(1), when it provides for the continuation of regular payments on Carol's student loan debts directly to those creditors while paying other unsecured nonpriority claims pro rata; and (2) whether Debtors are failing to commit 100% of their disposable income to their Amended Chapter 13 plan when Debtors Schedule J includes payment on a horse trailer of $141.00 per month, payment of $60.00 per month for the lease of roping steers, and payment for other business expenses of $290.00 per month. This

Memorandum of Decision sets forth the Court's findings of fact and conclusions of law.

FACTS

Robert is employed as a highway designer with the State of Montana, Department of Transportation. Carol is employed as a teacher by the East Helena School District. Debtors have an 18-year old son who is a senior in high school. Debtors filed their voluntary Chapter 13 petition on September 3, 2004. Debtors schedules filed September 3, 2004, list assets of $337,234.74 and liabilities of $320,979.83.

Robert's primary source of income is derived from his employment as a highway designer and engineering technician with the Montana Department of Transportation. Robert's current monthly gross wage is listed at $3,349.88 on Schedule I. When questioned by the Trustee, Robert stated that the monthly gross income figure of $3,349.88 includes estimated monthly income of $1,300.00 or $1,400.00 from the operation of Debtors' sideline business. Robert also represented, upon questioning by the Trustee, that the monthly income figure of $389.00 listed as regular income from the operation of a business was attributable to the sale of hay and cattle. Upon prompting by his counsel on redirect, and contrary to his previous answers to questions propounded by the Trustee, Robert testified that the monthly gross wage figure of $3,349.88 was solely attributable to his employment with the Department of Transportation. Robert also changed his answer with respect to the monthly income from the operation of a business, stating that the income figure of $389.00 per month was projected gross income less expenses, except for the expenses specifically enumerated on Schedule I.

Carol is employed as a teacher and earns a gross salary of $2,721.09 per month. After deducting payroll taxes, insurance, union dues and retirement contributions, Debtors' net monthly take home pay is $4,122.16. As noted above, Debtors' Schedule I also includes $389.00 per month under regular income from the operation of a business, profession or farm. Thus, Debtors' total monthly projected income is $4,511.16.

Per Schedule J, Debtors' monthly expenses total $4,361.11, which amount includes $88.00 per month for student loan payments, $141.00 per month for payments on a horse trailer, $60.00 per month to lease roping steers, and $290.00 per month for horse feed, vet shots, entry fees and shoeing.

According to Robert, Debtors operate a sideline horse training and roping business. Robert explained that his involvement with horses started when Robert was a "little kid". When Robert got out of school in 1963, he became a professional jockey and pursued that career until 1982, when Robert was seriously injured. Robert and Carol now train performance horses and Robert does team roping. Robert and Carol operate their sideline horse business with the intent of earning a profit. Debtors' 18-year old son is also involved in team roping and is a member of his high school rodeo team.

Robert testified that Debtors' horse business has "broke even" during the past few years, even though Debtors' showed a loss from the operation of their business on their 2002 and 2003 federal income tax returns. Robert explained that the loss shown on Debtors' tax returns is attributable to depreciation on equipment. According to Robert, "if we didn't have the depreciation on our equipment, we probably would have broke even on our business, and possibly even showed a profit." Upon retirement from the Department of Transportation, Robert would like to pursue his sideline horse business on a full-time basis.

Robert estimates that Debtors will earn, during the term of Debtors' plan, approximately

$1,300.00 to $1,400.00 in gross revenues per month from the operation of the horse business.

Contrary to Robert's testimony, Schedule C of Debtors' 2003 Federal income tax return reflects that Debtors' business realized gross receipts or sales of $2,485, or roughly $207.00 per month. Debtors' 2003 Schedule C also reflects that Debtors' reported a loss of $10,161 from the operation of their horse business, of which only $4,018 is attributable to depreciation. As the foregoing numbers reflect, Debtors' lost $6,143, exclusive of depreciation, in 2003 from the operation of their business. Similarly, Schedule C of Debtors' 2002 Federal income tax return reflects that Debtors realized gross receipts of $3,120 in 2002 from the operation of their horse business. The gross receipts in 2002 were offset with expenses totaling $20,937 for a loss of $17,817. Of the foregoing loss, $7,628 was attributed to depreciation resulting in a cash loss of $10,189. When Robert was pressed by the Trustee to explain the foundation for his belief that Debtors would realize gross revenues of $1,300.00 to $1,400.00 per month from the operation of the horse business–given the historical losses in 2002 and 2003--Robert merely characterized 2003 as a "bad year" and stated that he was injured in 2002. Robert's belief that Debtors will earn $1,300.00 to $1,400.00 per month from the operation of their business is premised solely on the fact that Robert said he has earned that much in the past and even won $2,500.00 during one roping event on an undisclosed date in an undisclosed year. Robert, however, failed to substantiate his statements with any corroborating evidence.

As previously discussed, when questioned by the Trustee, Robert was not able to reconcile his assertion that Debtors would realize gross revenues of $1,300.00 to $1,400.00 per month from the operation of their horse business with Debtors' Schedule I, where Debtors project that their regular income from the operation of their horse business will be $389.00 per month. Once again, Debtors' counsel stepped in and guided Robert to the response that the income figure of $389.00 was net of expenses, except of coarse, for the expenses specifically enumerated on Schedule J.

With regard to the monthly horse trailer payment of $141.00, Robert testified that Debtors' son uses the horse trailer. Debtors' son started roping when he was eight and qualified this past year for the High School Nationals. Debtors' son is once again looking forward to going to Nationals and if he performs well during the next several months, Debtors are hopeful that their son will secure a college scholarship. Robert stated that he and his wife cannot afford to send their son to college absent a scholarship. Robert thus stressed that it was imperative that Debtors keep their horse trailer.

Moving on, Debtors' Schedule F lists $82,765.83 in unsecured nonpriority claims, including a $8,667.00 claim owed to the Student Assistance Foundation. According to Proofs of Claim Nos. 1, 2 and 3, the Student Assistance Foundation assigned Carol's student loan obligations to MGSLP. As previously noted, MGSLP has filed three claims for unsecured nonpriority claims totaling $7,774.14.

Debtors have not filed objections to the allowance of the claims filed by MGSLP. Carol testified that she incurred the student loan obligations between 2000 and 2002 while completing her masters program. The three student loan obligations have been consolidated and Carol's monthly payment is $88.00 at an annual interest rate of 3.37 percent (APR) (3.37%). Carol testified that her student loan interest rate is the lowest rate available. Carol also testified that she has been told that if she stops making regular monthly payments on her student loan obligations, her interest rate would increase by 30 percent. Carol testified that she is current on her student loan payments.

Debtors' Schedule J provides for a monthly payment of $88.00 for Carol's student loans and consistently, Debtors' proposed Amended Chapter 13 Plan provides at paragraph 2(e) that "[t]he Trustee will make no payments to ECMC for Debtors' student loans." Carol testified that she would like to have her student loan debt paid off within 7 years. She stated that she would like to continue to make regular monthly payments on her student loan debt for "rehabilitation" and Debtors would like their son to have the ability to obtain student loans if needed. Carol explained that if Debtors' son needs student loans to attend college, Debtors would like to assist their son by at least co-signing on any student loans that their son may apply for in the future. Carol also mentioned that failure to repay the student loan obligations could impact Debtors' ability to retire.[1]

On cross examination by the Trustee, Carol conceded that Debtors could successfully make their plan payments without separate classification of the student loans. Carol also admitted that she has not explored obtaining a deferment of her student loan debt.

DISCUSSION

The Trustee first objects to confirmation of Debtors' Amended Chapter 13 Plan, arguing that the Plan unfairly discriminates among the unsecured class of creditors in violation of 11 U.S.C. § 1322(b)(1), because of proposed payments of $88.00 per month on student loan obligations. Discrimination among classes of unsecured claims is governed by 11 U.S.C. §

---

[1] Carol did not explain how her student loans would impact Debtors' ability to retire. The Court presumes that Carol was implying that Debtors' may not be able to make the $88.00 per month payment from their retirement benefits.

1322(b)(1) which provides that a plan may "designate a class or classes of unsecured claims . . . but may not discriminate unfairly against any class so designated; however, such plan may treat claims for a consumer debt of the debtor if an individual is liable on such consumer debt with the debtor differently than other unsecured claims." The Ninth Circuit Bankruptcy Appellate Panel ("BAP") noted: "By its own terms, § 1322(b)(1) allows for discriminatory treatment among classes of creditors, as long as that treatment is not unfair." *In re Labib-Kiyarash*, 271 B.R. 189, 192 (9th Cir. BAP 2001) (citing *In re Sperna*, 173 B.R. 654, 658 (9th Cir BAP 1994)). The BAP held that a debtor may use 11 U.S.C. § 1322(b)(5) to maintain long-term student loan payments at the contract rate while curing any arrearage through the plan, provided that the plan satisfies the test for unfair discrimination under § 1322(b)(1) set forth in *Amfac Distribution Corp. v. Wolff (In re Wolff)*, 22 B.R. 510 (9th Cir. BAP 1982). *Labib-Kiyarash*, 271 B.R. at 195.

According to the evidence in the record, Debtors' Amended Chapter 13 Plan does not attempt to cure a default or arrearage in student loans, because Carol is current on her loan payments. Rather, Debtors simply seek to continue making Carol's regular monthly student loan payments in the amount of $88.00. In *Wolff* the BAP recognized that "there will be occasions where unsecured claims might be classified and treated differently, even though the legal character of the claims is identical and the treatment is discriminatory, but not unfairly so," and adopted four factors to consider when determining whether discrimination is "unfair":

> (1) whether the discrimination has a reasonable basis;
> (2) whether the debtor can carry out a plan without the discrimination;
> (3) whether the discrimination is proposed in good faith; and
> (4) whether the degree of discrimination is directly related to the basis or rationale for the discrimination.

Wolff, 22 B.R. at 512; *In re Labib-Kiyarash*, 271 B.R. at 192. This Court followed the *Wolff* factors in *In re Carlson*, 19 Mont. B.R. 390, 393, 276 B.R. 653, 655-66 (Bankr. D. Mont. 2002). *See also In re Demarais*, 20 Mont. B.R. 272, 275 (Bankr. D. Mont. 2002) and *In re Pegar*, 20 Mont. B.R. 494 (Bankr. D. Mont. 2003). However, in *Carlson*, the Court cautioned that "due to the factual nature of the analysis required under the *Wolff* test and the fact that such test does not provide a great degree of predictability or guidance, the Court is still of the belief that the determination of whether discrimination among creditors is unfair must be made on a case-by-case basis." *Carlson*, 19 Mont. B.R. at 396, 276 B.R. at 658. Particularly important in this case is the fact that Debtors have the burden of proving that the separate classification does not unfairly discriminate against the other unsecured creditors. *See In re Labib-Kiyarash*, 271 B.R. at 195; *Carlson,* 19 Mont. B.R. at 396, 276 B.R. at 658; *Demarais*, 20 Mont. B.R. at 275-76; *Pegar*, 20 Mont. B.R. at 499.

The first *Wolff* factor is whether the discrimination has a reasonable basis. By itself, nondischargeability of a claim such as a student loan does not provide a reasonable basis for discrimination. *Carlson*, 19 Mont. B.R. at 394, 276 B.R. at 658; *Labib-Kiyarash*, 271 B.R. at 196. In order for discrimination to have a reasonable basis it must advance the purposes behind Chapter 13. *Demarais*, 20 Mont. B.R. at 276; *Pegar*, 20 Mont. B.R. at 500; *Carlson*, 19 Mont. B.R. at 394, 276 B.R. at 657; *Sperna*, 173 B.R. at 658. In *Sperna* the BAP noted the purpose behind Chapter 13 includes affording debtors a fresh start, protecting assets and discharging obligations not excepted from discharge, while at the same time maintaining a balance with other Congressional policy considerations. 173 B.R. at 659. One of those public policy considerations established by Congress is that student loans be repaid. *Sperna*, 173 B.R. at 659; *see also In re Sullivan*, 195 B.R. 649, 655 (W.D. Tex. 1996).

The BAP noted that factors such as special provisions for the collection of student loans "might be relevant" to justify disparate treatment, but the debtors in *Sperna* did not present any evidence demonstrating that such factors could affect their plan. *Sperna*, 173 B.R. at 659. Likewise in *Carlson*, the debtors offered absolutely no basis for their desire to discriminate in favor of student loans during the last 2 years of a 5-year plan. 276 B.R. 653. Similarly, in the instant case, other than the fact that Carol's interest rate on her student loans will increase from 3.37% to 4.49%,[2] Debtors failed to articulate any compelling reason for discriminating among their unsecured creditors. Carol stated that if their son goes to college and needs a student loan, Debtors would like to have good credit in order to co-sign for their son. However, neither Carol nor Robert could state with certainty whether Debtors could indeed co-sign on a loan for their son given the fact that Debtors filed bankruptcy. Additionally, based upon Robert's testimony, their son's ability to attend college is first dependent upon their son securing a rodeo scholarship.

In sum, Debtors' testimony regarding possible adverse consequences resulting from failure to maintain their student loan payments fails to provide the same detail as provided by the debtors in *Demarais*, 20 Mont. B.R. at 276-77, and *Pegar*, 20 Mont. B.R. at 500. In *Demarais*, this Court approved the proposed discrimination where the debtor presented evidence that payment of his student loans through the plan, as opposed to making regular payments, would prompt collection action by the student loan creditor, and would result in penalties upon reinstatement of the loan at the end of the debtor's plan, including a lump sum payment to cover all missed payments. *Demarais*, 20 Mont. B.R. at 276-77. Therefore, in *Demarais*, the Court

---

[2] The difference in the two interest rates multiplied by the total of Carol's student loan obligations results in a monthly impact upon Debtors of less than $13.00.

determined that the proposed discrimination advanced the purposes of Chapter 13 by providing the debtor with a fresh start. In contrast to *Demarais,* the testimony in this case simply establishes that the only certain adverse consequence is that the interest rate on the student loan obligations will increase to approximately 4.49 percent if Debtors have to pay the student loan obligations through their Chapter 13 plan on a pro rata basis with other unsecured debt.

It was not only the threat of collection activities and the imposition of penalties which provided a reasonable basis for the proposed discrimination in *Demarais*, but also the Congressional policy that student loans be repaid, which the plan proposed to continue, and the debtor's intention to purchase a home by keeping his student loan payments current. *Demarais*, 20 Mont. B.R. at 276-77. Based upon these facts, the Court found that the debtor satisfied the first *Wolff* factor by showing that the proposed discrimination had a reasonable basis. *Id*, 20 Mont. B.R. at 277. The facts in *Pegar* prompted a similar conclusion. *Pegar*, 20 Mont. B.R. at 500-01. In the instant case, the Court finds that Debtors have not satisfied their burden of proof by showing that their Plan advances the purposes behind Chapter 13. *Carlson*, 19 Mont. B.R. at 394, 276 B.R. at 657; *Sperna*, 173 B.R. at 658. Consequently, Debtors have not satisfied the first prong of the *Wolff* test.

Factor two of the *Wolff* test considers whether the debtors can carry out a plan without the discrimination. Under this factor, bankruptcy courts should examine "what payments were due under the loan agreements, when the last payment was due under the loan agreements in relation to the plan, whether there were any arrearages, whether the loans have been accelerated and whether the plans would effect an acceleration." *Demarais*, 20 Mont. B.R. at 277; *Pegar*, 20 Mont. B.R. at 502; *Carlson*, 19 Mont. B.R. at 394, 276 B.R. at 657 (quoting *Sperna*, 173 B.R. at

659). Carol testified that Debtors are current on Carol's long-term student loan payments of $88.00 per month. Notwithstanding, upon examination by the Trustee, Carol admitted that Debtors could fulfill the terms of their plan without the separate classification of student loan debts. Such an admission in this case is determinative. Debtors have failed their burden with respect to factor two of the *Wolff* test.

As to factor three, the BAP instructs that "an appropriate view of good faith under the *Wolff* test is whether the discrimination involved furthers the goals of the debtor, satisfies the purposes behind Chapter 13 and does not require any creditor or group to bear an unreasonable burden. For example, if the plans were being used to effectively accelerate payments on the loans at the expense of the unsecured creditors, such discrimination would be in bad faith." *Demarais*, 20 Mont. B.R. at 279; *Pegar*, 20 Mont. B.R. at 504; *Sperna*, 173 B.R. at 660; *Carlson*, 19 Mont. B.R. at 395, 276 B.R. at 657.

Debtors' plan proposes to maintain the regular long-term monthly student loan payments of $88. However, given Debtors inability to articulate a sound reason for the discrimination, the Court can only conclude that the discrimination is proposed for the sole purpose of maintaining payments on a nondischargeable debt to the detriment of other unsecured creditors. Consequently, the Court finds that Debtors have also failed their burden as it relates to the third *Wolff* factor.

The final *Wolff* factor is whether the degree of discrimination is directly related to the basis or rationale for the discrimination. In *Sperna*, the BAP clarified its distinction between factor 2 and factor 4 as follows: "The second factor asks whether any discrimination at all is necessary. If the answer is affirmative, the court must then determine if the amount, or degree, of discrimination proposed is directly related to the reason for the discrimination." *Demarais*, 20 Mont. B.R. at 279-80; *Pegar*, 20 Mont. B.R. at 505; *Sperna*, 173 B.R. at 660; *Carlson*, 19 Mont. B.R. at 395, 276 B.R. at 657.

This Court has already determined that Debtors do not have a sound basis or rationale for the proposed discrimination. Thus, it is impossible for Debtors to show that the degree of discrimination is related to the basis or rationale for the discrimination.

This Court has previously articulated its belief that the determination of whether discrimination among creditors is unfair under § 1322(b)(1) must be made on a case-by case basis. *Demarais*, 20 Mont. B.R. at 280; *Carlson*, 19 Mont. B.R. at 393, 276 B.R. at 658. The Court has wide discretion in making this determination. *In re Labib-Kiyarash*, 271 B.R. at 196; *Demarais*, 20 Mont. B.R. at 280; *Carlson*, 19 Mont. B.R. at 396, 276 B.R. at 658.

In *Carlson* the debtors offered no evidence in support of their proposed discrimination. *Carlson*, 19 Mont. B.R. at 399, 276 B.R. at 660. In *In re Pearson*, 20 Mont. B.R. 507, 509-10 (Bankr. D. Mont. 2003), the debtor offered mostly his attorney's argument, without personal knowledge of the effect default would have without the discrimination. Similarly, the Debtors in this case offered too little evidence to satisfy the *Wolff* factors. Exercising its wide discretion, the Court concludes that Debtors have not satisfied their burden of proving that the separate classification of Carol's regular long-term student loan payments does not discriminate unfairly against the other unsecured nonpriority claims. *In re Labib-Kiyarash*, 271 B.R. at 195; *Wolff*, 22 B.R. at 512; *Demarais*, 20 Mont. B.R. at 281.

In *In re Thibodeau*, 248 B.R. 699, 706 n.6 (Bankr. D. Mass. 2000) (cited in *In re Labib-Kiyarash*, 271 B.R. at 193-94), the court recognized that it could not force the debtor to extend her plan beyond the 36 month minimum, but suggested that the debtor could choose to extend the plan term up to 5 years allowing greater distribution to other general unsecured creditors. *See, e.g., Carlson*, 276 B.R. at 659. As in *Thibodeau*, the Debtors in this case could potentially justify their proposed discrimination by extending their plan beyond 36 months. Debtors, however, have not made such a proposal. Accordingly, Debtors' proposed discrimination is denied.

Next, the Trustee asserts that Debtors are not contributing 100% of their disposable income to their plan as required by 11 U.S.C. § 1325(b)(1)(B). Section 1325(b)(1) of the Bankruptcy Code provides that if an unsecured creditor or the trustee objects to confirmation of a Chapter 13 plan, and the plan does not provide for 100% payment to all unsecured creditors, then a debtor must commit all disposable income to the plan. Section 1325(b)(2) defines the term "disposable income" as:

> --income which is received by the debtor and which is not reasonably necessary to be expended–
>
> > (A) for the maintenance or support of the debtor or a dependent of the debtor, including charitable contributions (that meet the definition of "charitable contribution" under section 548(d)(3)) to a qualified religious or charitable entity or organization (as that term is defined in section § 548(d)(4)) in an amount not to exceed 15 percent of the gross income of the debtor for the year in which the contributions are made; and
> >
> > (B) if the debtor is engaged in business, for the payment of expenditures necessary for the continuation, preservation, and operation of such business.

11 U.S.C. § 1325(b)(2); *In re Cavanagh*, 18 Mont. B.R. 109, 111-12, 242 B.R. 707, 710 (Bankr. D. Mont. 2000), *aff'd*, 18 Mont. B.R. 351, 352, 250 B.R. 107, 110-11 (9th Cir. BAP 2000); *In re Sutton*, 19 Mont. B.R. 220, 228 (Bankr. D. Mont. 2001); *In re Eiesland*, 19 Mont. B.R. 194, 204 (Bankr. D.Mont. 2001). Whether particular expenses or expenditures qualify as "reasonably

necessary" depends on the facts and circumstances of each individual case. *In re Shaffer*, 15 Mont. B.R. 286, 288 (Bankr. D. Mont. 1996).

The initial inquiry in the instant case is whether Debtors' sideline horse business is an actual business or merely a hobby or recreational endeavor. In a seminal case, the United States Supreme Court has held that a taxpayer's gambling activities were a business and that his losses were therefore deductible. The Court ruled:

> We accept the fact that to be engaged in a trade or business, the taxpayer must be involved in the activity with continuity and regularity and that the taxpayer's primary purpose for engaging in the activity must be for income or profit. A sporadic activity, a hobby, or an amusement diversion does not qualify....[W]e conclude that if one's gambling activity is pursued full time, in good faith, and with regularity, to the production of income for a livelihood, and is not a mere hobby, it is a trade or business....We therefore adhere to the general position ... that resolution of this issue requires an examination of the facts in each case.

Commissioner of Internal Revenue v. Groetzinger, 480 U.S. 23, 35-36, 107 S.Ct. 980, 94 L.Ed.2d 25 (1987) (citations and quotation marks omitted). The Internal Revenue Service subsequently adopted Treas.Reg. § 1.183-2, setting forth nine criteria to be considered in determining whether an activity was business or recreational in nature. As explained by the Second Circuit Court of Appeals:

> Under the regulations enacted pursuant to the statute, "[a]n activity is engaged in for profit if the taxpayer entertained an actual and honest, even though unreasonable or unrealistic, profit objective in engaging in the activity." *Campbell v. Commissioner of Internal Revenue*, 868 F.2d 833, 836 (6th Cir.1989); Treas.Reg. § 1.183-2(a). The regulations direct that a taxpayer's intent be divined "by reference to objective standards, taking into account all of the facts and circumstances of each case." Treas.Reg. § 1.183-2(a); *Estate of Baron v. Commissioner of Internal Revenue*, 798 F.2d 65, 74 (2d Cir.1986). The regulations list nine factors that normally should be considered: (1) whether the taxpayer carried on the activity in a businesslike manner; (2) the expertise of the taxpayer or his advisors; (3) the time and effort expended by the taxpayer in conducting the activity; (4) the expectation that assets used in the activity may

> appreciate in value; (5) the taxpayer's success in carrying on similar or dissimilar activities; (6) the taxpayer's history of income or loss in the activity; (7) the amount of occasional profits earned, if any; (8) the taxpayer's financial status; and (9) elements of personal pleasure or recreation in the activity. *See id.* at § 1.183-2(b)(1)-(9). These factors are not exclusive, and no one factor or number of factors is determinative. *Id.; Hendricks v. Commissioner of the Internal Revenue Service*, 32 F.3d 94, 98 (4th Cir.1994); *Faulconer*, 748 F.2d at 894. The burden of demonstrating that an activity was engaged in with the requisite profit motive rests with the taxpayer. *Welch v. Helvering*, 290 U.S. 111, 115, 54 S.Ct. 8, 9, 78 L.Ed. 212 (1933); *Burger v. Commissioner of Internal Revenue*, 809 F.2d 355, 358 (7th Cir.1987); *Faulconer,* 748 F.2d at 893.
>
> Although the regulations reflect Congress's desire for an objective standard to evaluate a taxpayer's profit motive, *see, e.g., Nickerson*, 700 F.2d at 405, their emphasis on a case-by-case consideration of circumstances and the explicit rejection of a mathematical weighing of factors indicate that common sense and an appreciation for the overall picture also must play a role in answering the elusive question of a particular taxpayer's intent.

Ranciato v. Commissioner of Internal Revenue, 52 F.3d 23, 25-26 (2^{nd} Cir. 1995).

In the case *sub judice*, Robert testified that he has been involved with horses for the better part of his life. The evidence shows that Robert has carried on his roping and horse training activities in a businesslike manner. Robert obviously has a great deal of expertise when it comes to horses and he, Carol and Debtors' son all appear to expend a great deal of time and effort working with horses. Robert testified that Debtors' roping and horse training business also provides Robert's sole source of recreation and helps maintain Robert's mental and physical health. After considering the foregoing, the Court concludes that Debtors are engaged in a valid business and that their activities are not a mere hobby.

The Court's next inquiry is thus whether the expenses set forth on Debtors' Schedule J that are associated with Debtors' horse business are reasonably necessary for the maintenance and support of Debtors and their son. The Court was originally inclined to hold that the expenses associated with Debtors' horse business as set forth on Schedule J are reasonably necessary for the maintenance of Debtors and their son. The Court's initial inclination was premised on the fact that Debtors have listed income of $389.00 per month to offset various of their itemized expenses, namely, $141.00 per month for the horse trailer, $60.00 per month to lease steers and $290.00 per month for horse feed, vet shots, entry fees and shoeing. Also, at first blush, it did not appear that Debtors' Schedule J was riddled with questionable expenses. For instance, Debtors have scheduled a measly $4.75 per month for recreation. Additionally, unlike many debtors, the Debtors in this case appear to have foregone such items as internet access and satellite or cable television. Debtors have not budgeted anything for charitable contributions and Debtors' monthly food bill for 3 people is a reasonable $350.00 per month. Again, at first blush, it did not appear that Debtors were attempting to pad their expenses. Additionally, it did not appear that Debtors were attempting to lead a life of luxury at the expense of their creditors. Finally, the Court was, and is, very concerned that it does not take any action that would thwart Debtors' son's ability to attend college.

However, after considering Debtors' testimony and after reviewing the record, the Court finds that Debtors are not being completely forthright with the Court, the Trustee or their creditors. Robert testified that Debtors expect to earn between $1,300.00 and $1,400.00 per month from the operation of their horse business. Upon very leading questioning by Debtors' counsel, Robert testified that his projection of $1,300.00 to $1,400.00 is reflected in the $389.00 of income set forth on Schedule I. Apparently, the income of $389.00 is net of various expenses not already listed on Schedule J.

In reviewing Schedule C of Debtors' 2003 U.S. Individual Income Tax Return, Exhibit A, the Court notes that Debtors deducted $2,273 last year for car and truck expenses. Those expenses are already itemized on Debtors' Schedule J under auto insurance, installment payments on their automobiles (which amount contains an interest component) and transportation. Debtors' also deducted $120.00 for the rental of business property, which the Court presumes relates to the roping steers. Once again, such expense is already deducted at the rate of $60.00 per month on Debtors' Schedule J. Other expenses listed on Debtors' Schedule C of their 2003 tax return relate to taxes and licenses, horse hay, entry fees, shoeing horses, feed, vet supplies and "Feed and Sup for Ste." The foregoing expenses already appear to be deducted on Debtors' Schedule J. Schedule C of Debtors' 2003 tax return also deducts $682.00 for one-half of meals. This amount should also be reflected under "Food" on Debtors' Schedule J as Robert testified that Debtors sleep and eat in their horse trailer.

Using the expenses set forth on Schedule C of Debtors' 2003 tax return and disregarding the above expenses, which are already set forth on Debtors' Schedule J, Debtors should have total other annual expenses of $1,428.00 consisting of $100.00 for legal and professional services, $543.00 for repairs and maintenance, $465.00 for supplies, $240.00 for dues and $80.00 for panels and steers. Dividing the remaining expenses of $1,428.00 by 12 months results in a deduction of approximately $119.00 per month for the various other expenses not already listed on Debtors' Schedule J. Subtracting $119.00 from Robert's projection that Debtors will earn between $1,300.00 and $1,400.00 per month from the horse business means that Debtors should have listed their monthly business income at $1,181.00 per month, rather than the $389.00 listed by Debtors on Schedule I.

Utilizing the foregoing numbers, the Court finds that Debtors' monthly income is potentially understated by $792.00 due to a double counting to Debtors' business expenses. Such amount equates to $9,504.00 over a 12-month period. Debtors assert in their Response to the Trustee's objection that Debtors' business operation also saves Debtors $3,500.00 per year in taxes. Debtors' disposable income is thus understated by $9,504.00 less $3,500.00, or $6,004.00–$500.00 per month. The foregoing amount is suspiciously similar to the sum of the expenses scheduled by Debtors on Schedule J for the "trailer payment", "lease steers" and "horse feed, vet short, entry fees, shoeing", which items total $491.00 per month.

The Court is deeply troubled by the fact that it appears Debtors are attempting to deduct their expenses in two different fashions, once on Schedule I and once on Schedule J, in an effort to avoid paying their creditors. The line on Schedule I where Debtors have listed their business income at $389.00 specifically requires Debtors to attach a detailed statement. Debtors did not attach a detailed statement itemizing their business income and expenses. Moreover, Debtors listed "0.00" on Schedule J under "Regular expenses from operation of business, profession, or farm."

The fact that Debtors' Schedules simply do not "add up" compels this Court to require Debtors to include the trailer payment, the lease payment on the steers and the horse fee, vet shots, entry fees and shoeing expenses in Debtors' disposable income calculation. The Court enters such ruling reluctantly and hopes that Debtors' son is not adversely impacted by this decision. Nevertheless, the facts in this case do not permit the Court to enter any alternative ruling. As the amended plan is a 36-month plan, this memorandum does not consider the analysis advocated by *In re Mendoza*, 274 B.R. 522, 525 (Bankr. D. Ariz. 2002).

In accordance with the foregoing discussion, the Court finds that Debtors have $3,782.11

in allowable expenses under 11 U.S.C. § 1325(b)(2). Such expenses totaling $3,782.11 are reasonable and necessary for the maintenance and support of Debtors. Accordingly,

IT IS ORDERED the Court will enter a separate Order sustaining the Trustee's Objection to confirmation of Debtors' Amended Chapter 13 Plan; denying confirmation of Debtors' Amended Chapter 13 Plan; and granting Debtors ten (10) days from the date of this Order to file a Second Amended Chapter 13 plan.

IT IS FURTHER ORDERED that in the event Debtors fail to timely file a Second Amended Chapter 13 plan, the Court will enter an order dismissing this case without further notice or hearing.

IT IS FURTHER ORDERED and NOTICE IS HEREBY GIVEN that if Debtors timely file a Second Amended Chapter 13 plan, a hearing on approval of said plan shall be held on Tuesday, February 8, 2005, at 09:00 a.m., or as soon thereafter as the parties can be heard, in the 2ND FLOOR COURTROOM, FEDERAL BUILDING, 400 N. MAIN, BUTTE, MONTANA.

BY THE COURT

Ralph B Kirscher

HON. RALPH B. KIRSCHER
U.S. Bankruptcy Judge
United States Bankruptcy Court
District of Montana